How to Negotiate a Winning Term

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It's not entirely unimaginable that startups, even with mentors guiding them, can end up signing contracts that could haunt them for 7-8 years, typically a startup's lifecycle.

Negotiating with investors and reaching mutually agreeable term-sheets are the 'Achilles heels' of startup entrepreneurs. After 2-3 years of starting up, several entrepreneurs realise that their efforts were unlikely to pay back anything substantial because of clauses they agreed to.

The ill-advised clauses prevent several of them from leaving the companies they established unless they agreed to give up everything. "Entrepreneurs often tend to focus on only one thing - valuations, for example - to the exclusion of other clauses," said Mukul Gulati, principal at investment firm SAIF Partners. "They have to have a balanced view, and have to be more cognizant of their rights." Investors say they appreciate entrepreneurs prepared with a bank of alternative options before approaching them for capital; it shows their seriousness to the exercise of fund-raising. "It's always advisable to consult mentors and advisers before you negotiate with an investor.

We investors have done over 100-150 deals but it may be the first one for the startup entrepreneur," said Arpit Aggarwal, principal at Blume Ventures. An entrepreneur would do well to have a best alternative to a negotiated agreement, or BATNA, ready before approaching an investor - a Plan B or even a C. "You must protect every ounce of equity in the company as hard as you can. Ultimately, it's not a salary you are working for, but the reward at the end of it through sale of your shares, or control in the company," said Deepak Menaria, founder and CEO of Nagpurbased Lemon School of Entrepreneurship, an incubator for startups in small towns.

It's always advisable to pick the right battles, say experts. Founders should not agree to dilute more than 30% equity in any round, said Navin Kumar Rungta, cofounder and CEO of eLagaan, a startup advisory and compliance firm. "People should just walk away from deals which take over 50-60%," said Rungta. "There is nothing called a a standard term-sheet. We often ask VC investors if it's a 'standard' it should have been published somewhere. Such investors have no answer."

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